Capital

Shall We Export It or Use It for American Business?

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FOREIGN trade for the United States is both necessary and desirable. There is no disagreement on this point among bankers, business men, economists, statesmen. However, in seeking a lead for the revival of American business, attention should not be focused on foreign trade to the exclusion of domestic business. American exports have constituted only some six to eight per cent of the total sales of this country during the period of maximum exports. The domestic market is definitely under American control, to be revived if proper thought and action are taken. A clear ray of hope offers in the thought that measures looking toward business revival can be taken at home and at once. This does not mean that foreign trade, particularly in certain commodities, is not important. It does mean that the key to business revival lies in the domestic market and a more normal foreign trade than that of the calendar years 1915–1920.

The Place of Foreign Trade in American Business

The basic factors which determine the character and scope of a country's foreign trade will operate to cause the United States to seek out certain commodities needed and to export commodities in the production of which the United States has the greatest comparative advantages.

The climate of the United States prevents the production of certain commodities needed, such as tea, coffee, raw silk, rubber, cocoa, sisal, jute. These must be bought in the countries where they can be produced. It so happens that the products denied the United States by climatic conditions are found in tropical countries which want and do not produce the commodities this country can and does produce. Direct trading with such countries is therefore natural.

The United States can export goods in the production of which it has the greatest comparative advantages, due to climate, natural resources and the genius of the American people for organization and quantity production. In resources the United States excels in iron, silver, lumber, copper and other well-known basic materials. Soil and climate combine to give an advantage in the production of such goods as grain, cotton, meat and dairy products. The genius of Americans has found characteristic expression in the mass production of standardized articles, particularly of iron and steel. It also has found expression in such devices as cash registers, adding machines, typewriters, sewing machines and many similar articles of clever invention. It seems reasonably clear that whatever is the peculiar product of the climate of the United States may be sold everywhere by Americans in the face of any competition. Whatever product is benefited by peculiarity of American resources, either great supply or accessibility, may likewise be sold against competition. It is probably not too strong a statement to say that whatever is the peculiar product of American genius—whether genius for

invention, mass production or business organization—may be sold by Americans in the face of competition. These influences not only make possible but even compel the export of certain goods.

In sum, the United States can sell in any open market the commodities in the production of which it excels. There will be an interchange of goods with those countries which can supply products needed and require American goods. There will be a continuing pressure to export goods to Europe. Though the total value of exports to Europe has shrunk, the United States will continue to look to Europe to purchase cotton and other products which have so long been marketed there. Indeed, it seems reasonably certain that the United States will have a favorable balance of trade with Europe for some time, though appreciably less than indicated by export figures for the war and after-war period.

It scarcely needs to be said that foreign markets must be available in the years ahead for those commodities which have comprised the major portion of the export trade of the United States during the period 1914–1920. Heading the list of these commodities are raw and manufactured cotton, manufactures of iron and steel, breadstuffs, meat and dairy products and mineral oil. It seems likely, however, that this export trade of the United States will conform more and more to the value, volume and trend of such trade during the period 1900–1913, rather than to the export trade built up through war conditions.

In determining the place of foreign trade it is just as important to emphasize the point that foreign trade is both necessary and desirable for the United States as it is to emphasize a second point, which seems sometimes to be overlooked, that a continuation of abnormal exports cannot be expected. American exports mounted both in value and volume to unprecedented proportions, particularly during the years 1915–1920. But once the stimulation of extraordinary demand and dire necessity were withdrawn, there was a noticeable drift back to trade more in alignment with pre-war trends. Any notion that the United States can go on indefinitely selling all kinds of goods in all markets at fancy prices finds no confirmation in the views of experts who have studied conditions or in foreign trade statistics.

The prospect for the revival of American business lies in the increase of business in the domestic markets and in a foreign trade maintained along more natural lines and developed in a more normal way than is sometimes urged by the proponents of plans for the artificial stimulation of foreign trade. Ultimately, of course, if (also when and as) European countries pay the interest due the United States on their borrowings and try to amortize their debts, these payments will be made largely in goods and an unfavorable trade balance, or stream of merchandise imports in excess of merchandise exports, must be expected. Any long time appraisal of foreign trade solely in terms of exports is faulty. Close thinking must compass the problem of imports—and tariffs.

In approaching the problem of business revival, it is true that account must be taken of the fact that although the export trade of the United States has constituted only some six to eight per cent of total sales during the years when exports were at their height, this comparatively small volume of sales has a disproportionate significance, particularly with respect to those commodities in the production of which the United States enjoys distinct advantages. Export trade conforming more

closely to the "doctrine of comparative costs" is as inevitable as it is desirable.

Before developing the remaining points in this paper, that Europe should take steps to help herself and that the export of capital has a distinct effect on business revival, it is necessary to sound the warning that such arguments set up no brief against the position that natural trends of foreign trade are necessary for the United States.

WHAT EUROPE SHOULD DO

The world, as a community of nations engaged in trade, is in an ill-balanced financial position. The United States, and in much less degree Great Britain, are the only countries with an appreciable amount of capital for export. For the purpose of maintaining their own financial solidity, these two countries can ill-afford to supply Continental Europe with funds secured through bank expansion. In fact, they can properly urge that the Continental countries take steps to straighten out their finances as a matter of good faith, if nothing more, before seeking extensive financial aid.

Reports indicate that the nations of Continental Europe have made small progress in balancing their budgets. Deficits have accumulated. These nations must make serious efforts to improve public finances. This course involves stringent measures in the way of deflating inflated paper currencies. It also involves taxation of the most rigorous character. There must be retrenchment in public expenditures. Internal funding loans of greater proportions will doubtless be necessary to reduce floating debts,—particularly to reduce debts to the state banks of issue so as to bring about a reduction in the volume of outstanding bank notes. It seems clear that European nations—some more than others—must do all these things. But more, they must put such restrictions on imports as to bar out goods that are not vitally necessary for their rehabilitation. It is imperative that the European countries work, tax, save, restrict imports to necessities,—and above all reverse the mad policy of printing bank notes. On these points economists are in agreement.

If Continental Europe does not show a disposition to put her house in order, it is not too much to suggest that British and American financiers, as well as the governments of Great Britain and the United States, should exert at least moral pressure to bring about this result. The United States could even lay down as a condition precedent to its financial coöperation or aid, serious and intelligent efforts at financial and monetary rehabilitation by the countries of Europe.

It is not amiss to note that efforts to correct the ill-balanced financial position of European countries will affect the volume of American exports to Europe. These exports are now diminishing because of the high premium the dollar commands in other currencies. The point should not be lost sight of that one of the chief influences affecting exchange rates are differences in the price levels in different countries. It has been demonstrated in fact as in theory that the parity of exchange between two countries is affected by the purchasing power of the monies of those two countries. If inflation is not checked or appreciably reduced, exchange rates must obtain which will operate as a barrier to the exportation of American goods to Europe. If France, for instance, makes no serious effort at deflation, and America is successful in its deflationary process, the ratio between the price levels in the two countries will show an

even wider disparity, and buying by France in America will be increasingly difficult. It is probably safe to say that variation in price levels, monetary standards and politics now have a major influence on foreign exchange,—a greater influence than trade balances.

One of the conditions necessary for normal trading between the United States and Europe is, therefore, that European countries shall themselves take clearly defined steps to strengthen their exchange position. Moreover, Europe should first help herself before seeking large amounts of new capital in the American market. This is necessary as a matter of good faith, as a common sense way of strengthening her position with regard to making securities attractive in the American market.

THE EXPORT OF AMERICAN CAPITAL

The extent to which European nations have been securing capital in the American market may not be fully comprehended. During the period 1915–1920, foreign loans floated through American bankers aggregated some five billion dollars. Direct loans by the Federal Government to European nations amounted to some ten billion dollars. At the present time the unfunded debt of Europe probably amounts to somewhere between three and one-half and four billion dollars. In all, these figures represent an export of something like nineteen billions of capital.

To show the significance of these figures a comparison may be noted. During the period 1915–1920, the total reported issues of securities—railroad and traction, industrial, municipal and state, and those put out by the Federal Government—amounted to forty-three and one-half billion dollars. Of that total, fifteen billion dollars went to Europe. Europeans received three billions more than were given to all American railroads, traction companies and industries combined. They received as much as these with state and municipal issues added.

Justification for proposals to furnish Europe with even more capital is sought in the plea that the fortunes of the people of the United States are tied up with those of Europe. Failure, distress and disaster there will mean failure, distress and disaster here. The view is urged that American goods, particularly raw materials, must be sold to Europeans, not only in order to relieve the American market, but also to furnish Europe the materials on which to work in the process of economic rehabilitation. Any proposal to furnish Europe with more capital should receive the closest scrutiny.

In many statements regarding the subject of exporting capital, the idea seems to be prevalent that money is the only form of capital. If the United States makes loans to France and the proceeds of the loans are expended in the United States, it is felt that Americans will be safe because the money is still here. But in such case they have parted with capital *goods* which have been paid for with their own funds. They will receive for these capital goods the customary evidences of debt—bonds or notes which draw interest. This is as truly an export of capital as if gold had been sent abroad, and Americans have identical evidence in either case. American capital resources have been depleted to the same extent in either case. It is immaterial whether the recent hundred million dollar French loan was made in goods or in gold so far as this country's capital account is concerned. Thinking about the export of capital should not be confused by centering attention on money and forgetting the fact that capital goods are exported even though

the money may be spent in this country.

Much the same situation underlies the plan for the proposed Hundred Million Dollar Foreign Trade Financing Corporation. It is a plan to export some part, or all, of a billion dollars worth of capital chiefly to Europe. It is a plan to stimulate exports, but it involves the export of capital goods in return for which Americans would receive interest bearing promises to pay.

The reluctance of many of the larger banks to furnish capital for the organization of this Corporation in such large amounts as have been asked, is no doubt due to the knowledge bankers have of the enormous losses sustained by foreign financing companies during the last eighteen months, and the further knowledge of the fact that almost every foreign dock has been filled with goods which have not been accepted by foreign buyers.

It is a matter of common knowledge that European nations owe the United States Government about ten billion dollars. Payment of the principal amount is regarded in some quarters as problematic. Payment of the interest charges has been deferred. But if payment is made of both principal and interest, such payment must be made largely in goods, that is, the balance of trade over a number of years must run in favor of the obligated nations and be unfavorable to the United States. Under the circumstances it is possible to understand the argument in favor of the cancellation of the debt owed by European nations to the Federal Government. However, it seems unlikely that any such proposal can be seriously entertained, both because it is contrary to the trend of public opinion in the United States and because it might not be acquiesced in abroad. Therefore, the long run view of the effect of capital advances to Europe and the payment of interest and principal must compass the question of imports and ultimate unfavorable trade balances.

Even if proposed plans for financing Europe are not brought to the point of execution, the prevention of foreign raids on American capital resources is worthy of serious thought. The German war indemnity bonds are an illustration.

It is reported that on July 1, Series A of the German war indemnity bonds to the amount of three billion dollars will be issued. Series B, nine billions in amount, will be issued November 1 next. The interest rate will be five per cent. Series C bonds will amount to twenty-one billion dollars and will be issued under detailed provisions which need not now be considered.[1] The United States will receive none of these bonds, nor indemnity payments of any kind. Nevertheless, the governments that do receive the bonds will probably try to market them in the United States as it is the only great, unrestricted investment market. European nations will command new American capital to the extent that the bonds are bought by American investors.

In any discussion of America's part in European rehabilitation, the question of the export of capital from America is a primary, not a secondary matter. This fact has already been shown by the large amount of capital furnished Europe—some nineteen billions of dollars. The promoters of the Hundred Million Dollar Foreign Trade Financing Corporation have urged that the United States is morally bound to help Europe and selfishly concerned in developing export trade if it would maintain or revive domestic

[1] For a detailed statement regarding the issuance of the German indemnity bonds, see the article by Mr. McDonald in this volume.—[Ed.]

prosperity. But no plan has yet been proposed that does not in effect provide merely for the wholesale granting of commodity credits.

In connection with this or other proposals to furnish Europe with capital, it goes without saying that persistent refusal to coöperate in any way with Europe would have a serious reaction on industry in the United States. About this point there can be no doubt. However, the United States owes to Europe, as well as itself, the duty of keeping its house in order. If the United States does not do the best it can with its own resources it will do less than is possible for Europe. In considering foreign trade and the export of American capital, not only the needs or demands of Europe must be taken into account, but also the capacity of Americans to export capital without seriously affecting domestic industry. Europe would not gain in the long run from the impairment of American resources and capital. Too much emphasis can be placed on what America can do for Europe and not enough on what Europe can and must do for herself. European countries owe America the duty of righting their economic position by strong adherence to sound and sane rules of financing, taxation and fiscal operations. It is important that attention be given the needs of Europe for capital, but it is necessary also to consider American needs.

America's Need of Capital

No recourse to statistics is really necessary to confirm the truth of the statements so often made that American railroads have not received, for several years, adequate additions to their capital—additions which were necessary to efficient transportation service. It is common knowledge that renewals, additions and betterments are needed. Some idea of the situation, however, can be gained from the fact that reported issues of railroad and traction securities from 1909 to 1914 averaged almost one billion dollars each year, while from 1917 to 1920 inclusive, the average was less than four hundred and fifty million dollars a year. It seems a reasonable inference that the export of American capital to Europe must have helped to stay railroad progress and development. Similarly, the export of American capital must have had an adverse effect on building operations and must have been a contributing cause to the present housing shortage. Capital needs for building are problematic. Estimates range from one to five billion dollars. Even the most conservative figures, however, show the need for capital in the United States if building is to play its full part in the restoration of domestic prosperity. Indeed, in every field of domestic endeavor the shortage of capital, evidenced by high interest rates, has been more or less seriously felt and although the United States is now a creditor nation, it must be recalled that at no time in its history, prior to the war, have the people of the United States accumulated enough capital for American needs. The United States was regularly a debtor nation.

Interest Rates

Business men in the United States have been greatly disturbed over high interest rates. Bankers, however, are not to be charged with the responsibility for this condition. There has not been enough capital to meet the demand at low interest rates. Bidding for the available supply of capital has been vigorous and always in competition with hard-pressed European countries. The prospect of lower interest rates is remote unless the demand for

capital subsides to a great extent, or unless capital accumulations are greatly increased. With Europe still bidding for capital, interest rates are not likely to take a marked and immediate downward trend. Prior to the war, the average amount of new securities issued, recorded and unrecorded, is estimated at three billion dollars a year. During and since the war, it is estimated that these issues have averaged six billions and yet apparently they have not been sufficient to meet capital demands at a low rate of interest. With a lower and lowering price level, domestic capital requirements should diminish, but there will also be a diminution in capital accumulations measured in terms of dollars. The probable trend of interest rates, so closely related to the export of American capital, raises the question of the capacity of the American people to save.

SAVINGS NOT INDEFINITELY ELASTIC

If the savings of the American people were indefinitely elastic, there would be no problem connected with the export of American capital. There would be no particular problem of interest rates. The hard fact, however, is that savings are not indefinitely expansible. The amount of capital accumulated depends on the national income and the capacity and disposition of the people to save.

Any nation's income has limits. For 1917 the best estimates fixed the total income of the American people at fifty to sixty-five billion dollars. Assuming twenty million families at that time and a bare subsistence cost of living for each at a thousand dollars a year, twenty billion dollars were needed for what may be called a "human maintenance fund." This fund is certainly not less today. Out of the remainder of whatever the national income may be must come all expenditures for comforts, luxuries, taxes and also capital, whether for American industry or for foreigners, or both.

In considering the possible savings of the people of the United States it is helpful to divide the total number of families into income groups. Families with incomes of $1,500 or less can save practically nothing. Families whose incomes range from $1,500 to $5,000 are disposed to spend rather than save, after making their customary investments in insurance and homes. Families with incomes above $5,000 have had their resources eaten into by income and surtaxes. While the greater proportion of capital accumulations during the period 1900 to 1910 came from the last named group and from corporation surpluses, income and profits taxes have cut heavily into what might otherwise have been industrial capital. If the tax program of the United States could be radically revised, this source of capital would be restored, but it seems unlikely that such modification of tax rates will be made as to restore the position of the well-to-do or corporations with respect to this matter of furnishing capital. With the savings power of the high income group seriously impaired, and the low income group without financial leeway, dependence for capital rests more largely on the middle income group—families with incomes from $1,500 to $5,000 a year.

If savings cannot be indefinitely increased, the question arises, "To what use shall capital accumulations be put?" Shall they be turned in large measure to Europe or put to work in the United States? Since savings are not indefinitely expansible, a decision is necessary as to whether they shall be spent here to furnish Europeans with capital goods, or spent here to furnish American industries with such capital goods.

Or perhaps the question should be put thus, To what extent shall American savings be used to furnish Europe with capital goods and to what extent used to furnish capital goods for the rehabilitation of American industries? One thing at least seems clear. The United States cannot export its capital and have it too.

The evident purpose of the proponents of the various plans for financing Europe is to sell American goods,—hence the suggestion that capital advances be conditioned on the expenditure of the funds in American markets. Thus, any real or supposed surplus of goods can be reduced or disposed of—at a price. This plan was followed during the war with the result that there has been an accumulation of Europe's obligations in this country on which interest charges may be paid, but there is no general and confident expectation of the prompt repayment of the principal. The point must not be lost sight of that if payment is made, it will be made chiefly in goods. Europe's purpose in seeking American capital is probably to buy not manufactured products beyond immediate needs, but rather raw materials and equipment. With these her labor can produce finished products to be sold back to the United States or to other countries, perhaps in competition with America.

The scheme of financing sales to Europe would be more alluring if a revival of business on the high price level of the first part of 1920 could be foreseen. But the maintenance of such a price level is neither possible nor desirable. It has already been lowered everywhere. The revival of American business on the basis of lower prices is inevitable. If the price of goods is to be lower, costs must be lowered enough to give a reasonable margin of profit. This applies not only to production for the domestic market but production for foreign markets. The lowering of costs demands a higher degree of efficiency in production. This higher efficiency must be found in capital as well as labor. There must be the use of adequate and efficient capital equipment. American transportation, in particular, has capital needs that must be met. It is important, therefore, in fact of major importance, that the question of business revival be considered in relation to the problem of the extent to which American capital should be exported.

THE REVIVAL OF AMERICAN BUSINESS

The main thread of the argument in this paper is that the revival of American business will be worked out on the basis of the domestic market and a more normal foreign trade. In turning attention to domestic trade the question of capital needs at home must receive attention. In considering American export trade, due regard must be had not only for schemes for financing that trade, but also for the "doctrine of comparative costs." Full thought must likewise be given to the correction of monetary conditions in Europe through deflation, taxation and economy. The fact must not be overlooked that Europeans must restrict imports. If European nations are to deflate their currencies, pay taxes and work, they will have less demand for anything from the United States other than what aids them to manufacture goods and sell them chiefly in the American market. If certain of the European nations are impoverished, their position will not be greatly improved by America's financing sales of goods without adequate consideration of the risk involved or thought of the extent to which capital should be exported. If Europe is impoverished,

improvement of the condition of her peoples will not be brought about by forcing America to the same condition.

Foreign trade has been emphasized to such a degree of late that thought of business revival is largely in terms of exports and foreign financing. If it were necessary for the people of the United States to await the rehabilitation of Europe before they could enjoy a fuller measure of prosperity, they might have to wait a very long time. Just how long, no one knows! Such a prospect is far from comforting at a time when gloom enough engulfs American business. It was in the hope that a shift of emphasis from foreign to domestic trade would carry a message of encouragement, that this paper was prepared. An American perspective shows that measures at home can and should be taken. There need be no paralysis of action with the world's greatest domestic market at hand and controllable. To emphasize this point, an exaggerated statement might almost be risked, that if we take care of our ninety-two or ninety-three per cent of domestic business, the seven per cent of foreign business will take care of itself.

This is calculated to be a message of comfort and cheer to all who have not lost the power of self-help. What is needed is courage, straight thinking, the restoration of a sound moral code, —but above all, *action*.

American Trends in Foreign Trade

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THE United States is facing extraordinary conditions with respect to foreign trade and finance, but beneath these extraordinary conditions may be seen indications of the working of natural tendencies. Foreign trade cannot indefinitely remain abnormal.

When a movement to "capture" foreign markets was started, there were a few maligned authorities who advised caution, a policy of careful progress rather than hasty plunging into the intricacies of foreign trade by those who were not sufficiently equipped with practical knowledge of the conduct of that trade. British and European papers did not scoff at American efforts to capture markets. Many of them, however, did point out that the United States would show wisdom in adhering to the development of foreign commerce along lines with which it was familiar. The history of England's overseas commerce proves that foreign trade is of slow and tedious growth, not springing overnight into full bloom as many American merchants and manufacturers apparently expected.

The foreign trade of the United States during the years of the war, and in fact until the latter part of 1919, was not dependent on real trading or salesmanship. Goods were asked for and supplied, the main object being the satisfaction of demands as quickly as possible. Such trading is not normal.

Indirect or triangular trading, if it comes at all, is likely to be of long and slow development. The trend of foreign trade of the United States has been direct. English shipping has a large proportion devoted to "tramp trading," a proportion estimated at more than fifty per cent of its mercan-